United States Court of Appeals

for the Second Circuit

APPELLANT'S PETITION FOR REHEARING

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

DOCKET NO. 74-1697

SIRBO HOLDINGS, INC.,

Petitioner, Appellant,

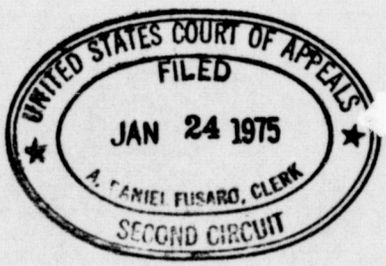
v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent, Appellee.

ON APPEAL FROM THE UNITED STATES TAX COURT

APPELLANT'S PETITION FOR REHEARING AND/OR PETITION FOR REHEARING EN BANC



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PRELIMINARY STATEMENT

Appellant hereby petitions the Court for rehearing of its judgment, entered in this case on January 14, 1975, and as grounds therefor respectfully shows the following points of fact and law that in the opinion of Appellant the Court has overlooked or misapprehended.

I

The Court overlooked evidence in the record bearing on allocation of the $125,000 payment, as between capital gain and ordinary income elements.

The Court held: that the $125,000 payment received by Sirbo from CBS contained two elements (or might have contained such elements), first, a payment for removal or destruction of Sirbo's property such as theatre seats, carpeting, chandeliers, stage curtains, and various structural features of the theatre, and, second, a payment equivalent to the cost of removing the property of CBS such as control booths and the stage apron extension; that the payments for Sirbo's property constitute sales or exchanges of property used in Sirbo's trade or business within the meaning of §1231(a) and therefore entitled to capital gains treatment, but that any payments for the removal of property of CBS were not payments for property used in Sirbo's trade or business and therefore were not entitled

to capital gains treatment; that appellant made no effort to supply an allocation of the $125,000 as between the two elements possibly included therein; that because of Sirbo's failure to supply such an allocation the Court affirms the decision of the Tax Court that the entire $125,000 payment constituted ordinary income.

The Court overlooked the evidence presented at the original trial of this case as to how the $125,000 figure had been arrived at. This consisted of testimony of Mr. Myron Boyce, an officer of the Appellant, which appears at pages 40-65 of Appellant's Appendix in Docket No. 72-1617, the testimony of Milton L. Maier, a former employee of CBS who actually negotiated the $125,000 figure in behalf of CBS, which appears at pages 86-91 of Appellant's Appendix in Docket No. 72-1617, and Exhibit 12, an appraisal made for CBS by one John J. McNamara, a theatre architect, upon the instructions of Mr. Maier, which appears at page 191 of Appellant's Appendix in Docket No. 72-1617. The substance of the testimony by Mr. Boyce was that Sirbo obtained estimates of the various costs involved in restoring the leased premises to its November 14, 1947 condition which totalled approximately $200,000, which amount it claimed from CBS under the lease restoration clause, and that CBS presented to Sirbo a detailed estimate of such costs in the amount of $70,000, which estimate had been prepared by the architect, McNamara, and that the parties had negotiated and arrived at a

compromise figure of $125,000. Mr. Maier's testimony generally substantiated the testimony of Mr. Boyce. Mr. Maier further testified that in requesting the estimate from Mr. McNamara (both of them were engaged in protecting CBS's interests) he asked McNamara for his estimate of a "minimum job". In view of the testimony that the $125,000 figure represented a compromise based on itemized estimates totalling $200,000, on the one hand, and $70,000, on the other hand, it was impossible for Appellant to present evidence as to precisely how much of the $125,000 constituted the capital gain element referred to in this Court's opinion for the reason that the parties never broke down the $125,000 figure. It is most significant, however, that the detailed McNamara estimate which is in evidence and which totalled $70,000, contained no amount for removal of the property of CBS. From this it must be inferred from the record that not less than $70,000 represented payment for Sirbo's property used in its trade or business. For the convenience of the Court Appellant has included a copy of the detailed McNamara estimate at the end of this petition.

III

Whether or not the Court, upon reconsideration, agrees that the evidence referred to above was sufficient to support an allocation, the Court misapprehended the extent of Appellant's burden of proof before the Tax Court.

Helvering v. Taylor, 293 U.S. 507 (1935) holds that, in

the Tax Court, and in appeals from the Tax Court, a taxpayer does not have a burden of establishing either that no tax is due from him, or his "correct" tax liability; the burden on a Tax Court petitioner is discharged by his showing that the Commissioner erred in the statutory deficiency determination which is the peculiar basis of Tax Court jurisdiction.

In Taylor an individual taxpayer had purchased stock of various utilities for $96,030, which utilities stock he transferred to a holding company in exchange for all the latter's preferred and common stock. The holding company later retired such preferred stock, by itself, for $99,000. On his return the individual shareholder treated $96,030 of this $99,000 as a return of capital, in effect attributing all his original cost "basis" to the preferred and nothing to the common, reporting as gain only the difference of $2,970. The Commissioner rightly concluded that the taxpayer had to apportion his cost "basis" between the preferred and common. Nevertheless, although the Commissioner was clearly right in insisting upon such apportionment, the Commissioner's actual apportionment of basis in his deficiency determination was itself "unfair and erroneous" resulting in an "excessive" tax. Notwithstanding, the Tax Court [then the Board of Appeals] sustained the Commissioner's "erroneous" deficiency determination. The Court of Appeals for the Second Circuit reversed. On certiorari

the Supreme Court summarized as follows[1] the now discredited position of the Commissioner concerning the taxpayer's burden of proof before the Tax Court"

> "His contention is that in this case the burden on the taxpayer was not only to prove that the Commissioner's determination is erroneous, but to show the correct amount of the tax. In substance he says that, because of the taxpayer's failure to establish facts on which a fair apportionment may be made, the Board's redetermination at the Commissioner's erroneous figure was valid, and, there being no error of law, should have been sustained by the court."

The Supreme Court rejected this contention of the Commissioner, allegedly based on the then applicable Revenue Act of 1926, stating:

> "Plainly it does not support the Commissioner's contention that the taxpayer, even though he has shown the determination to be arbitrary and excessive, must nevertheless pay the added tax because he has not also shown that he owes nothing or the correct amount, if any, that legally may be laid upon him."

The Supreme Court also rejected the Commissioner's arguments based on the procedural rule that the taxpayer had the burden of proof before the Tax Court. The Supreme Court defined the burden on a taxpayer before the Tax Court as one of proving that the Commissioner was wrong in his deficiency determination--not the greater

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[1] 293 U.S. at pages 512-514

burden of proving no tax was due or the"correct amount" of tax due. Referring to Rule 30 of the Tax Court's then Rules of Practice, the Supreme Court stated:

> "But there is nothing in it to suggest intention to require the taxpayer to prove not only that a deficiency assessment laid upon him was arbitrary and wrong, but also to show the correct amount.
>
> * * *
>
> "We find nothing in the statutes, the rules of the Board of our decisions that gives any support to the idea that the Commissioner's determination shown to be without rational foundation and excessive will be enforced unless the taxpayer proves he owes nothing or, if liable at all, shows the correct amount."

CONCLUSION

In this case the Commissioner erroneously determined that the entire $125,000 was all ordinary income, and no part of it was capital gain. The opinion of the Court of Appeals was that an undetermined part of the $125,000 represented capital gain from a "sale or exchange" and not ordinary income; but because the Court concluded that Sirbo had failed to prove a precise allocation, the Commissioner's "erroneous" allocation, in effect, of zero (to any capital gain element) must be sustained. This, however assumes Sirbo's burden of proof to be greater than it was. Sirbo's burden was fully discharged by proving the Commissioner's determination "erroneous".

In any event this record contains clear evidence, apparently overlooked heretofore by the Court of Appeals, that at least $70,000 of the $125,000 (the $70,000 consists of the detailed estimate by CBS's expert theatre architect, McNamara) was attributable to the destroyed or removed property of Sirbo. The fact that Sirbo was unwilling to accept this $70,000 figure, and insisted on a higher figure (originally $200,000) ultimately compromised out at $125,000, cannot take away Sirbo's right to capital gain treatment for at least $70,000 of the $125,000.

The Court of Appeals should also note that the Tax Court (in its two prior opinions) makes no reference to the presumed unavailability in this record of materials on which a proper allocation of the $125,000 can be based. Cf. Cohan v. Commissioner, 39 F.2d 540 (C.C.A. 2, 1930).[2]

Respectfully submitted,

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[2]Especially pages 543, 544. In the instant case, as in Taylor, the Tax Court never came to this question of the burden of proof on apportionment of the amount at issue. 293 U.S. at page 514.

CERTIFICATION OF SERVICE

I hereby certify that service of this APPELLLANT'S PETITION FOR REHEARING AND/OR PETITION FOR REHEARING EN BANC was made on Respondent, Appellee on January 23, 1975, by mailing two copies thereof, postage prepaid, to its counsel at the following address:

Ernest J. Brown
Assistant Chief, Appellate Section
Tax Division
Department of Justice
Washington, D. C. 20530

James R. McGowan